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DEPARTMENT FOR EUR/SCE, EEB/IFD/OMA AND EEB/EPPD, TREASURY  
FOR OASIA LARRY NORTON

E.O. 12958: N/A

TAGS: [EFIN](#) [ETRD](#) [ECON](#) [HR](#)

SUBJECT: EARLY YEAR-END NUMBERS CONFIRM WEAKENING CROATIAN  
ECONOMY

REF: A. ZAGREB 20

[1](#)B. 2008 ZAGREB 872

[1](#)1. SUMMARY: Year-end figures confirm a slowdown in the Croatian economy. In the third quarter of 2008, GDP grew at its slowest pace in eight years, rising just 1.6 percent above its level in the third quarter of 2007. Retailers saw decreased sales in the second half of 2008, prompting significant job cuts should sales continue to slump into early 2009. Other businesses are now being hit by the Russian gas cutoff and a new law prohibiting most retailers from operating on Sunday. The most optimistic forecast for GDP growth in 2009 is now 1 percent, while some analysts say Croatia is facing recession. End summary.

[1](#)2. Data released in the last days of 2008 and the first weeks of 2009 confirm that the effects of the global financial crisis have reached the Croatian economy. Exports dropped and demand waned in the third quarter of 2008, helping to slow GDP growth to its slowest pace in eight years. GDP for the third quarter of 2008 was just 1.6 percent higher than in 2007, compared to 5.1 percent growth in 2007 over 2006. In November, the global economic turmoil helped to shrink Croatia's trade deficit as demand for imports dropped faster than exports. For the year 2008 as a whole, however, the current account deficit widened to more than 10 percent of GDP. The turmoil also hit the Zagreb Stock Exchange. With a 67 percent decline in share values, investors have proclaimed 2008 the worst year ever for the 17-year-old exchange.

[1](#)3. Retail sales turnover showed negative growth for much of the second half of 2008. The latest figures show that in November, retail sales were 11 percent lower than in October 2008, and 4 percent lower than in November 2007. The first week of January brought announcements of job cuts from retailers, banks and other sectors. The largest job losses were in the retail sector, due not only to the economic downturn but also to a new law banning most stores from opening on Sundays outside the Christmas and tourist seasons. Many retailers, as well as the opposition Social Democratic Party (SDP), have called for the government to revise or suspend the Sunday shopping ban, and several major retail chains have said they will file a lawsuit challenging its constitutionality.

[1](#)4. On top of these economic troubles, the cut in natural gas supplies due to the Russian-Ukraine dispute has forced many businesses to decrease or stop operations (reftel A). The GOC has not determined the total number of firms affected or estimated the extent of the damage. Press reports, however, say several hundred firms have been affected. A representative of the Croatian Employers Association (HUP) told one daily paper the damage could reach 1 billion EUR (\$1.3 billion) and deal "a final blow" to manufacturing in these already difficult circumstances.

15. At the end of December, the Croatian National Bank lowered its forecast for 2009 GDP growth from 2 percent to 1 percent (reftel B). Some private analysts are even less optimistic and have started to offer warnings of recession. An analyst with Raiffeisen Consulting told the press that fourth quarter data for 2008 could show negative GDP growth, and that 2009 could see as much as a 0.6 percent decline in GDP. GDP growth at these levels also could affect the government's 2009 budget, which assumes 2 percent growth in GDP. Early fiscal data for 2009 have not been promising. A leaked Ministry of Finance report showed budget revenues for the first two weeks of 2009 63 percent down from the same period last year. Minister of Finance Ivan Suker said last week that the government is not considering revising the budget at this point and intends to wait until data for the first several months of the year are available. According to press reports, however, Sanader's advisory Economic Council intends to propose budget revisions already at a session on January 23.

16. COMMENT: While Croatia successfully avoided fears of an immediate financial collapse last fall, and has won international praise for its sound monetary policies, the new data confirm fears that there will be significant pain to come. Expectations for the economy are now so low that even modest success in any sector will likely be lauded as a significant victory in the dim climate. With local elections looming in May, the government will be looking hard for any success to point to as it gears up for the campaign. END COMMENT.  
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